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No.

# In the Supreme Court

OF THE

# United States

OCTOBER TERM, 1984

GEORGE DEUKMEJIAN, Governor of the State of California, *et al.*,
*Appellants,*

VS.

NATIONAL MEAT ASSOCIATION, *et al.*,
*Appellees.*

**On Appeal from the United States Court of Appeals for the Ninth Circuit**

## JURISDICTIONAL STATEMENT

JOHN K. VAN DE KAMP
Attorney General of the State of California
R. H. CONNETT
Assistant Attorney General
RODERICK E. WALSTON
Deputy Attorney General
(Counsel of Record)
ALLENE C. ZANGER
Deputy Attorney General
6000 State Building
350 McAllister Street
San Francisco, CA 94102
Telephone: (415) 557-3920
*Counsel for Appellants*

BOWNE OF SAN FRANCISCO, INC. • 190 NINTH ST. • S.F., CA 94103 • (415) 864-2300

72 pp

## QUESTIONS PRESENTED

The California Legislature has adopted a State marketing program to stimulate beef sales in California. To finance the program, the Legislature imposed assessments on out-of-state processors who market beef in California to compensate for assessments imposed on California producers, under circumstances where the in-state and out-of-state assessments are ultimately borne by similarly situated competitors under actual marketing conditions.

1. Does the California assessment scheme discriminate against interstate commerce in violation of the Commerce Clause of the U. S. Constitution?

2. Under the Commerce Clause, does California have the right to impose assessments on out-of-state processors who have no physical presence in California?

## PARTIES BELOW

The appellants are: George Deukmejian, Governor of the State of California; John K. Van De Kamp, Attorney General of the State of California; and Clare Berryhill, Director of the California Department of Food and Agriculture.

The appellees are: National Meat Association; American Meat Institute; Armour Packing Company; Dubuque Packing Company; Iowa Beef Processors, Inc.; Land O'Lakes, Inc.; Litvak Meat Company, Inc.; MBXL Corporation; Monfort of Colorado, Inc.; E. A. Miller & Sons Packing Corp., Inc.; National Beef Packing Company; Pepper Packing Company; Sterling Colorado Beef Company; and Swift Independent Packing Company.

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## JURISDICTIONAL STATEMENT

## OPINIONS BELOW

The opinion of the U. S. Court of Appeals for the Ninth Circuit has not yet been officially reported, and is set forth at Appendix 1-16. The opinion of the federal district court is reported at 562 F.Supp. 357, and is set forth at Appendix 17-35.

## JURISDICTIONAL GROUNDS

This is an action for declaratory and injunctive relief regarding a California law that is alleged to violate the Commerce Clause of the U. S. Constitution. Federal jurisdiction exists under 28 U.S.C. § 1331. The U. S. Court of Appeals for the Ninth Circuit filed and entered its decision on September 21, 1984. App. 1. The notice of appeal was filed in the Court of Appeals on October 5, 1984. App. 36. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(2). See *John P. King Mfg. Co. v. City Council*, 277 U.S. 100, 102-104 (1928); *McCollum v. Board of Education*, 333 U.S. 203, 206 (1948).

## APPLICABLE FEDERAL LAWS

Article I, Section 8, Clause 3, of the U. S. Constitution provides:

> "The Congress shall have power . . . to regulate commerce with foreign nations, and among the several States, and with the Indian tribes. . . ."

## STATEMENT OF THE CASE

### 1. Nature of the Controversy

Because of declining beef consumption now and in the past, the beef cattle industry is in a depressed condition, both in California and nationally. To rescue the industry, the California Legislature in 1956 enacted the California Beef Council Law (CBCL) to stimulate beef sales in California. Cal. Food & Agricultural Code (CFAC) §§ 64501-64736. The CBCL authorizes the California Director of

Food and Agriculture (Director), assisted by an advisory board, to adopt a State marketing program to increase beef sales in California. *Id.* at §§ 64561, 64591, 64661.

To finance the State marketing program, the CBCL since 1956 has imposed a "head fee" on California cattle producers for each sale of each animal marketed in California. CFAC §§ 64691, 64692. In 1982, the Legislature raised the head fee to $1 per head, which represents a four-fold increase. CFAC § 64691. Simultaneously, the Legislature imposed a "mil assessment" on out-of-state processors who market beef in California. CFAC § 64713. The mil assessment is based on the weight of processed beef marketed in California. *Id.* The Legislature concluded that, since the out-of-state beef industry receives the benefits of the State marketing program, it should pay a fair share of the program costs. As a result of the mil assessment, all beef marketed in California, whether originating in California or other states, is subject to assessments under the CBCL, subject to minor exceptions not relevant here.

The Legislature imposed the mil assessment on out-of-state processors because actual marketing conditions make it impossible to impose an assessment on out-of-state *producers* to correspond to the local head fee. This is so because, when the out-of-state producer sells his cattle to the out-of-state processor, it is not known whether the product will be marketed in California; and when the product is marketed in California, it is not possible to trace the product to the original producer. App. 30; Stip. 14. Therefore, it is not possible to impose an assessment on out-of-state producers that is identical to the head fee paid by local producers.

Further, as the Ninth Circuit acknowledged, the *undisputed* evidence shows that out-of-state processors "pass back" the mil assessments to out-of-state producers under actual marketing conditions. App. 10. The pass back oc-

curs because of the disparity in market power between processors and producers, caused by long-term expansion of beef supplies in relation to market needs. Youde Dec. 2-8. As a result of the pass back, the instate and out-of-state assessments are ultimately borne by instate and out-of-state producers who are in direct competition with each other.

Under actual marketing conditions, the California industry bears a proportionately heavier burden than the out-of-state industry to support the State marketing program. The disproportionateness occurs because California producers pay a head fee for each sale of cattle; since two or three sales typically occcur prior to slaughter,[1] two or three producers typically pay head fees on the same animal. Staiger Dec. 2; App. 32; Stip. 12. On the other hand, the mil assessment levied against out-of-state processors cannot exceed the equivalent of a single head fee. CFAC § 64713. Therefore, the California industry pays multiple fees for the same product, but the out-of-state industry does not. As a result, the out-of-state industry contributes only 40% of the marketing program costs, even though it sells 60% of the beef marketed in California. App. 14 n. 4, 32-33.

The above marketing factors explain why the California Legislature did not impose an assessment on California *processors* to correspond to the out-of-state mil assessment. If such an assessment were imposed on California processors, the processors would pass back the assessment to California producers, Youde Dec. 2-8, who already pay multiple fees for the same animal. This result would increase the disproportionately heavy burden already borne by California producers. Thus, actual marketing conditions make it unreasonable to impose identical assessments on instate and out-of-state processors.

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[1]For example, the rancher may sell to a stocker operator, who may sell to a feedlot operator, who may sell to a slaughterhouse.

The assessments collected under the CBCL are used exclusively to support the costs of the State marketing program, and cannot be used for general governmental purposes. CFAC § 64696. As a result of the 1982 legislative amendments, the revenues available for the marketing program will increase from $350,000-800,000 annually to approximately $5.3 million annually, thus enabling the Director and the advisory board to substantially increase beef sales in California. App. 32; Anderson Dec. 8. The plaintiffs conceded below that they benefit from increased beef sales in California. Stip. 10.

**2. The Proceedings Below**

The plaintiffs, consisting of twelve out-of-state beef processors and two industry trade associations, filed an action against California in a federal district court, seeking injunctive and declaratory relief on grounds that the California assessment scheme violates the Commerce Clause of the U. S. Constitution. The plaintiffs alleged that (1) California lacks requisite "nexus" with out-of-state processors who do not have a physical "presence" in California, such as sales offices, sales personnel, and so forth;[2] and (2) the California assessment scheme discriminates against interstate commerce. The parties, by prearrangement, filed cross motions for summary judgment, supported by a stipulation of facts and supplemented by additional declarations and exhibits submitted by the parties. The parties stipulated that the case raises purely legal issues, and should be decided on summary judgment.

The district court granted California's motion for summary judgment, and denied the plaintiffs' motion. App. 35. On the nexus issue, the district court ruled that, although some plaintiffs do not have a physical presence in Cali-

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[2]Some plaintiffs have such a physical presence in California, and others do not. Def. Exh. 4.

fornia, sufficient nexus exists because California provides specific marketing benefits to interstate commerce. App. 22-25. On the discrimination issue, the district court ruled that the California industry pays a proportionately heavier share of the marketing program costs than the out-of-state industry; that out-of-state processors "pass back" the mil assessments to out-of-state producers under actual marketing conditions; that California levies an assessment on both the instate and out-of-state industries at the first practicable opportunity; that no alternative scheme is available by which California can assess interstate commerce for its fair share of the marketing program costs; and therefore that the assessment scheme does not discriminate against interstate commerce. App. 26-34. The plaintiffs appealed.

The Ninth Circuit reversed the district court on the discrimination issue. App. 16. The Ninth Circuit ruled that the assessment scheme was discriminatory because "out-of-state beef processors are taxed; their California counterparts are not." App. 8. Therefore, it was concluded, the assessment scheme has a "discriminatory effect" and "constitutes economic protectionism." App. 7. The court dismissed as "legally insufficient" the undisputed fact that out-of-state processors pass back the mil assessments to out-of-state producers, App. 11, and gave no weight to the fact that the instate industry bears a proportionately heavier burden than the out-of-state industry to support the marketing program. App. 14 n. 4. The court specifically refrained from reaching the nexus issue, App. 4, although it stated that California "probably confers a benefit on out-of-state beef processors and producers by encouraging the consumption of beef in California and, therefore, . . . the state may have a legitimate right to be compensated for rendering a beneficial service." App. 14. California filed a notice of appeal. App. 36.

## REASONS FOR GRANTING PLENARY CONSIDERATION

### INTRODUCTION AND SUMMARY OF ARGUMENT

This case raises significant questions concerning a state's right to assess interstate commerce to support state marketing programs that provide specific benefits to interstate commerce. The questions are (1) whether a state has the right to impose facially dissimilar assessments on local and interstate commerce, where the dissimilarities are justified by legitimate, non-protectionist state interests and where equality results under actual marketing conditions, and (2) whether a state has the right to impose assessments where the assessee lacks conventional "nexus" with the assessing state.

The Ninth Circuit, in holding that the California assessment scheme discriminates against interstate commerce, followed improper Commerce Clause analysis in two fundamental respects. First, the Ninth Circuit adopted a mechanical *per se* rule focusing solely on the face of the scheme rather than on extrinsic factors that justify it. Under its mechanical analysis, state laws imposing facially dissimilar local and interstate burdens are invalid *per se,* whether or not the dissimilarities are justified by non-protectionist state interests or actual marketing conditions. Under modern Commerce Clause analysis, however, a more flexible rule prevails. Under the modern rule, state laws imposing facially dissimilar burdens are constitutionally sustainable if the dissimilarities are justified by all relevant extrinsic factors, such as non-protectionist state interests or actual marketing conditions. More specifically, absolute equality of burden is not required if the state law is supported by a rational, non-protectionist basis and is the only reasonable means by which the state interest can be served. And, a state law is not discriminatory in any event if it produces equality under actual marketing conditions.

As shall be explained, the California assessment scheme meets this more flexible test. The scheme is supported by a rational, non-protectionist basis, for (1) the purpose of the scheme is to require interstate commerce to pay its fair share of the marketing program costs, not to protect local industry; and (2) the existing scheme is the only reasonable means by which California can require interstate commerce to pay its fair share of the costs. See pages 18-19, 20-22, *infra*. Therefore, absolute equality of local and interstate burdens is not required. In any event, the assessment scheme produces equality under actual marketing conditions, because the out-of-state assessments are ultimately borne by out-of-state *producers* who directly compete with California producers who pay the local assessments. See pages 19-20, *infra*. Therefore, the assessment scheme is justified by all relevant extrinsic circumstances and does not discriminate against interstate commerce. The district court below, following proper Commerce Clause analysis, sustained the assessment scheme by considering all relevant extrinsic factors. The Ninth Circuit overturned the assessment scheme by following a mechanical *per se* approach that ignored all such factors.

The second way in which the Ninth Circuit followed improper Commerce Clause analysis was by treating this case as a tax case rather than an assessment case, and by rigidly applying this Court's tax decisions to the instant controversy. In this case, California assesses interstate commerce for specific marketing benefits provided to interstate commerce, rather than taxes all persons within its jurisdiction to support the general costs of government. The state interest in assessment cases—where the state provides specific benefits to interstate commerce—is fundamentally different and stronger than the state interest in tax cases, where no such specific benefits are provided. Also, actual marketing conditions often make it difficult to serve the state interest in assessment cases by facially symmet-

rical schemes. For these reasons, the states should be afforded greater latitude in adopting assessment schemes that attempt to fairly apportion the costs of regulatory marketing programs among a local and interstate industry. This Court's tax decisions are thus not wholly apposite here, and this case presents issues that have never been decided by this court.

This case has significant economic consequences. California, with the largest population of any state in the nation, provides an important market to the out-of-state beef industry. Californians annually consume more than 5 billion pounds of beef, of which more than 60% consists of imports from the out-of-state industry.[3] If California is unable to assess the out-of-state industry here, the financial impact on California's marketing program will be devastating. The out-of-state industry currently contributes $2.1 million annually to support the marketing program, which represents approximately 40% of the program costs. App. 14 n. 14. If California cannot collect these fees, it will be unable to fully achieve the marketing program goal of substantially increasing beef sales in California.

More broadly, this case raises significant federal questions concerning a state's authority to assess interstate commerce for specific agricultural benefits—and indeed other kinds of benefits—provided by the state. Further, California administers approximately thirty other marketing programs that regulate and promote specific agricultural products, and is considering adopting similar assessment schemes for some such programs. The case thus has broad economic significance that transcends the State marketing program involved here.

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[3]This figure is derived from the fact that the California industry produces approximately 2.37 billion pounds of beef each year, see California Department of Food and Agriculture, "California Agriculture Summary: 1983," at 2, which represents approximately 40% of the total beef consumed in California annually. App. 14 n. 14, 32-33.

## I

## THIS CASE RAISES SUBSTANTIAL FEDERAL QUESTIONS CONCERNING THE PERMISSIBLE LATITUDE OF STATE SCHEMES THAT IMPOSE ASSESSMENTS ON INTERSTATE COMMERCE

### A. The Ninth Circuit's "Per Se" Rule

In this case, the California Legislature adopted an assessment scheme requiring interstate commerce to help support a State marketing program that provides specific marketing benefits to interstate commerce. The Ninth Circuit invalidated the scheme on grounds that it imposes *facially* dissimilar burdens on similarly situated "taxpayers" in local and interstate commerce. App. 8. The Ninth Circuit stated:

> "Out-of-state beef processors are taxed; their California counterparts are not." App. 8.

From this simple undisputed fact, the Ninth Circuit drew the conclusions that the assessment scheme has a "discriminatory effect," App. 7; "constitutes economic protectionism," *id.;* "treats out-of-state taxpayers differently from similarly situated in-state taxpayers," *id.;* and "gives a direct commercial advantage to local business." *Id.* According to the court, a "virtually per se rule of invalidity" applies with respect to state "tax" schemes that impose *facially* dissimilar burdens on similarly situated "taxpayers" in local and interstate commerce. App. 6, 7.

The Ninth Circuit disregarded all economic evidence showing that the California assessment scheme does not discriminate against interstate commerce under actual marketing conditions, and indeed is the only reasonable means by which California can require interstate commerce to pay its fair share of the marketing program costs. The Ninth Circuit, for example, dismissed as "legally insufficient" and "not controlling" the undisputed fact that, under actual marketing conditions, the instate and out-of-state fees are ultimately borne by similarly situated instate and out-of-state producers. App. 10-11. The court attached no

weight to the fact that the assessment scheme places a proportionately heavier burden on the local industry than the out-of-state industry. App. 14 n. 4.

The Ninth Circuit did, however, suggest an alternative scheme that would provide facial symmetry between instate and out-of-state assessments. App. 15. As shall be explained, the Ninth Circuit alternative would shift the marketing program costs from the entire industry to a single group of competitors, and would require such competitors to pay more than the equivalent of $1 per head of cattle. See pages 20-21, *infra*. These results contradict the legislative judgment that the marketing program costs should be spread across the entire industry, and that no single competitor should pay more than the equivalent of $1 per head of cattle. *Id.* Thus, the Ninth Circuit second-guessed the legislative judgment without clearly understanding the practical implications of its suggested alternative.

In effect, the Ninth Circuit, by striking down the assessment scheme on its face, adopted a mechanical *per se* rule in determining whether the scheme discriminates against interstate commerce. Under this *per se* rule, a state assessment scheme that imposes facially dissimilar burdens on local and interstate commerce is automatically invalid regardless of extrinsic factors that may justify it. To be sure, the Ninth Circuit stated that "facial discrimination . . . is not the decisive factor," App. 7, and purported to examine the assessment scheme "in light of its actual effect." App. 7. The Ninth Circuit's analysis of the "actual effect," however, was confined to the fact that the scheme *facially* "taxes" out-of-state processors but not local processors. App. 8. Therefore, although the Ninth Circuit purported not to adopt a *per se* rule, it adopted such a rule *de facto*.[4]

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[4]The Ninth Circuit's per se rule is not the same *per se* rule adopted by this Court in *Spector Motor Service, Inc. v. O'Connor*, 340 U.S. 602 (1951), and subsequently rejected in *Complete Auto Transit*,

As we now explain, the Ninth Circuit's mechanical *per se* rule departs from proper Commerce Clause analysis and leads to the wrong result in this case.

**B. Commerce Clause Analysis.**

In considering whether state laws discriminate against interstate commerce in violation of the Commerce Clause, this Court has not considered the question without examining whether the state laws are justified by all relevant extrinsic factors. To the contrary, this Court has held that state laws, although discriminatory on their face, are sustainable if justified by non-protectionist state interests that cannot be served by reasonable nondiscriminatory alternatives. In *Hughes v. Oklahoma,* 441 U.S. 322 (1979), this Court stated:

> "The burden to show discrimination rests on the party challenging the validity of the statute, but '[w]hen discrimination against commerce . . . is demonstrated, the burden falls on the State to *justify* it both in terms of the *local benefits* flowing from the statute and the *unavailability of nondiscriminatory alternatives* adequate to preserve the local interests at stake.'" 441 U.S. at 336, quoting from *Hunt v. Washington State Apple Advertising Comm'n,* 432 U.S. 333, 353 (1977) (emphasis added). See also *Dean Milk Co. v. City of Madison,* 340 U.S. 349, 354 (1951).

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*Inc. v. Brady,* 430 U.S. 274 (1977). The Ninth Circuit *per se* rule holds that extrinsic factors cannot be considered in determining the discriminatory effect of a facially inequal state scheme, and the *Spector* rule held that the states could not impose taxes against interstate commerce under any circumstances. Although the rules are thus different, the rejection of *Spector's per se* rule in *Complete Auto* indicates that mechanical *per se* rules are disfavored under the Commerce Clause, which supports the position asserted by California here.

In *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27 (1980), this Court stated:

> "However important the state interest at hand, 'it may not be accomplished by discriminating against articles of commerce coming from outside the State *unless there is some reason, apart from their origin, to treat them differently.*'" 447 U.S. at 36, quoting from *Philadelphia v. New Jersey*, 437 U.S. 617, 626-627 (1978) (emphasis added).

Therefore, the Commerce Clause does not require absolute equality of local and interstate burdens *per se*. Rather, inequality of burden creates a presumption that the state law is discriminatory, but the presumption can be overcome by a showing that the state law pursues non-protectionist goals by the only reasonable means available.

A similar analysis appears in this Court's decisions invalidating state tax schemes that discriminate against interstate commerce. In *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963), this Court invalidated a Louisiana tax scheme that subjected out-of-state manufacturers of oil well servicing equipment to the same tax rates applied to local *purchasers* of such equipment, rather than local manufacturers. The Court concluded that the tax scheme was not supported by "adequate justification," and indeed that Louisiana had made "no attempt to justify" the scheme at all. 373 U.S. at 71, 74. In *Bacchus Imports, Inc. v. Dias*, ..... U.S. ....., 82 L.Ed.2d 200 (1984), this Court invalidated a Hawaiian tax scheme that exempted certain Hawaiian-produced liquors from a tax applied to out-of-state-produced liquors. The Court concluded that the tax scheme had the transparent "purpose" of "encourag[ing] development of the Hawaiian liquor industry," 82 L.Ed.2d at 205, 209, and that this was insufficient justification to impose a heavier burden on the out-of-state liquor industry. *Id.* at 207-210. In *Boston Stock Exchange v. State Tax*

*Comm'n*, 429 U.S. 318 (1977), this Court invalidated a New York stock transfer tax that imposed lesser rates on instate transfers than out-of-state transfers. The Court held that the tax scheme "favor[ed] local commercial interests over out-of-state interests," 318 U.S. at 335, and noted that the Court viewed with "particular suspicion state statutes requiring business operations to be performed in the home State that could more efficiently be performed elsewhere." *Id.* at 336. The states' failure to justify their tax schemes in these cases left intact the presumption that they were protecting local interests rather than pursuing non-protectionist goals by reasonable means.[5]

Apart from whether a state law pursues non-protectionist goals by reasonable means, a state law may be adequately justified if it produces equality under *actual* economic conditions. This Court has consistently held that the discriminatory effect of state laws must be determined by their "practical effect" under actual circumstances, not

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[5]Similarly, in *Armco, Inc. v. Hardesty*, ... U.S. ..., 81 L.Ed.2d 540 (1984), this Court invalidated a West Virginia wholesale tax applied to out-of-state wholesalers but not local wholesalers. West Virginia attempted to justify the tax by arguing that West Virginia wholesalers who were manufacturers were subject to a local *manufacturing* tax. 81 L.Ed.2d at 545-546. This Court concluded that this fact, by itself, was insufficient to justify the tax because manufacturing and wholesaling are not "substantially equivalent events." *Id.* at 545. In this case, California argues that its assessment scheme is justified by several extrinsic factors not present in *Armco*, that assessment cases are fundamentally different than tax cases, and that the assessment scheme here is the only reasonable means by which interstate commerce may be made to pay its fair share of the marketing program costs. See pages 17-21, *infra*. Therefore, *Armco* is of limited relevance here.

In *Maryland v. Louisiana*, 451 U.S. 725 (1981), this Court invalidated a Louisiana tax scheme that subjected locally-produced gas to lesser rates than out-of-state-produced gas. Louisiana offered no explanation whatsoever for the dissimilar rates, and was clearly attempting to protect its own gas-producing industry.

their "formal language." See *Hughes v. Oklahoma, supra,* 441 U.S. at 322; *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 279 (1977); *Commonwealth Edison Co. v. Montana,* 453 U.S. 609, 615 (1981); *Mobil Oil Corp. v. Commissioner,* 445 U.S. 425, 443 (1980). In *Lewis v. BT Investment Managers, Inc., supra,* 447 U.S. at 37, this Court stated:

> "The principal focus of inquiry must be the practical operation of the statute, since the validity of state laws must be judged chiefly in terms of their probable effects."

In cases invalidating state tax schemes on discrimination grounds, this Court has considered the practical effect of the schemes under actual conditions. See, *e.g., Boston Stock Exchange v. State Tax Comm'n, supra,* 429 U.S. at 336 (New York stock transfer tax encouraged instate rather than out-of-state transfers); *Bacchus Imports, Inc. v. Dias, supra,* 82 L.Ed.2d at 208 (Hawaiian liquor tax scheme potentially encouraged consumers to switch from out-of-state-produced liquors to Hawaiian-produced liquors). Therefore, the Ninth Circuit patently erred in disregarding undisputed economic evidence showing that the instate and out-of-state assessments are ultimately borne by similarly situated competitors under actual marketing conditions, App. 10-11, and that the "practical effect" of the assessment scheme is thus nondiscriminatory.

As this Court has often noted, the ultimate danger against which the Commerce Clause guards is economic isolation and protectionism by individual states. " 'What is ultimate is the principle that one state in its dealings with another may not place itself in a position of economic isolation.' " *Philadelphia v. New Jersey, supra,* 437 U.S. at 623, quoting from *Baldwin v. Seelig,* 294 U.S. 511, 527 (1935). This Court has adopted a "virtually per se rule of invalidity" with respect to state laws that are "in reality 'simple economic protectionism.' " *Minnesota v. Clover Leaf Creamery,* 449 U.S. 456, 471 (1981), quoting from *Philadelphia v. New Jersey, supra,* 437 U.S. at 624. Whether

economic isolation and protectionism occur cannot be determined without reference to whether the state law is adequately justified, in the sense that it pursues nonprotectionist goals by reasonable means or produces actual equality in the market place. Axiomatically, if the state law is adequately justified, the state is not protecting local industry, and the dangers against which the Commerce Clause guards do not arise.[6]

Commerce Clause analysis is thus not dissimilar from analysis under the Equal Protection Clause, which holds that distinctions between similarly situated competitors are valid if supported by a "rational basis." See, *e.g.*, *Vance v. Bradley*, 440 U.S. 93, 97 (1979); *City of New Orleans v. Dukes*, 427 U.S. 297, 303 (1976); *United States R. R. Re-*

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[6]In fact, this Court has sustained state tax schemes imposing dissimilar burdens on local and interstate commerce where such dissimilarities were adequately justified. In *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937), this Court sustained state use taxes collected by out-of-state sellers that "compensate" for sales taxes levied against local sellers. Sales and use taxes are not levied against similarly situated competitors; the sales tax is generally levied against the seller, and the use tax—although collected by the seller—is generally levied against the buyer. See *Henneford*, 300 U.S. at 581 (use tax levied against buyer); Hartman, *State Taxation of Interstate Commerce* 167 (1953). Indeed, Justice Brennan has noted that, because sales and use taxpayers do not follow the same practice in "shifting" the tax to the buyer, "as a matter of economic fact the out-of-state use taxpayer is likely ultimately to incur a heavier burden than his in-state counterpart, the sales taxpayer." *Halliburton Oil Well Cementing Co. v. Reily*, *supra*, 373 U.S. at 76 (Brennan, J., concurring). The overall scheme is sustainable, Justice Brennan notes, because the Commerce Clause does not "ensure absolute equality of economic burden as between sales and use taxpayers." *Id.* at 76. In other words, "absolute equality of economic burden" is not required if the state is pursuing legitimate goals by reasonable means, rather than protecting local industry.

*tirement System v. Fritz,* 449 U.S. 175 (1980). In *Fritz,* this Court stated:

> " 'In the area of economics and social welfare, a State does not violate the Equal Protection Clause merely because the classifications made by its laws are imperfect. If the classification has some "reasonable basis," it does not offend the Constitution simply because the classification "is not made with mathematical nicety or because in practice it results in some inequality." [Citation omitted.] "The problems of government are practical ones and may justify, if they do not require, rough accomodations—illogical, it may be, or unscientific." [Citation omitted.]' " 449 U.S. at 175, quoting from *Dandridge v. Williams,* 397 U.S. 471 (1970).

To recapitulate, the Commerce Clause, rather than establishing a mechanical *per se* rule, creates a presumption that facially unequal burdens are unconstitutional, but the presumption can be overcome by a showing that the dissimilarities are justified by all relevant extrinsic factors, such as non-protectionist goals pursued by reasonable means or actual marketing conditions. Therefore, although a "virtually per se rule of invalidity" applies if the state law protects local industry, see *Minnesota v. Clover Leaf Creamery Co., supra,* 449 U.S. at 471, "absolute equality of burden" is not required if the state law is adequately justified and thus does *not* protect local industry. See *Halliburton Oil Well Cementing Co. v. Reily, supra,* 373 U.S. at 76 (Brennan, J., concurring). See note 6, *supra.* The district court below properly held that the Commerce Clause does not "erect a *per se* rule against differing treatment of similarly situated taxpayers," and that "a statute which treats similarly situated taxpayers differently may pass constitutional muster if the different treatment is adequately justified." App. 29. The district court, after analyzing all relevant extrinsic factors, concluded that the California assessment scheme is adequately justified and hence con-

stitutional. App. 25-34. The Ninth Circuit, following its *per se* analysis, overturned the assessment scheme by ignoring all extrinsic factors that justify it.

**C. Distinction Between Tax and Assessment Schemes.**

The district court's more flexible analysis rather than the Ninth Circuit's *per se* rule is particularly appropriate in determining the constitutional validity of state assessment schemes, as opposed to state tax schemes.[7] In assessment cases, the state regulates and promotes an industry product, and, as part of its regulatory program, assesses the industry that benefits from the program. In conventional tax cases, the state seeks revenue for general governmental purposes from all persons located within its jurisdiction. See, *e.g., National Bellas Hess, Inc. v. Illinois Dept. of Revenue,* 386 U.S. 753, 756 (1967). The state interest is fundamentally different and stronger in assessment cases—where the state provides specific benefits to interstate commerce—than in tax cases, where no such specific benefits are provided.

On the other hand, the state interest in assessment cases often cannot be served by facially symmetrical schemes, because actual marketing conditions often make it difficult to symmetrically apportion the assessments among the entire industry. In this case, for example, actual marketing conditions prevent California from imposing assessments on the out-of-state industry that are parallel to the

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[7] This Court has stated:

> "'A tax is not an assessment of benefits. It is . . . a means of distributing the burden of the costs of government.'" *Commonwealth Edison Co. v. Montana, supra,* 453 U.S. at 622-623, quoting from *Carmichael v. Southern Coal & Coke Co.,* 301 U.S. 495, 521-523 (1937).

Therefore, an "assessment of benefits" that does not distribute "the burden of the costs of government" is not a tax, at least in conventional form.

local assessments. See pages 2-3, *supra*. Thus, California faces a dilemma here that does not arise in conventional tax cases, because California has a clear right to assess interstate commerce but cannot adopt a reasonable parallel scheme. Therefore, California should not be held to the more rigid standard applied in conventional tax cases, such as *Boston Stock Exchange* and *Bacchus Imports*, where the states failed to show any legitimate interest in imposing dissimilar burdens on local and interstate commerce.

Therefore, this Court's tax decisions are not wholly apposite here. The Ninth Circuit, beyond misconstruing this Court's tax decisions, failed to appreciate that they provide only an imperfect analogy here, and that this case truly presents issues of first impression. Indeed, the Ninth Circuit continually referred to this case as a "tax" case, *e.g.*, App. 7, 8, 9, 10, overlooking the fundamental difference between tax and assessment cases under the Commerce Clause.

**D. Analysis of California Assessment Scheme.**

We now examine the California assessment scheme in light of the Commerce Clause principles described above. As shall be seen, the scheme is justified in light of all extrinsic factors and does not protect local industry. Specifically, the scheme is supported by a non-protectionist purpose; has a nondiscriminatory effect under actual marketing conditions; is supported by a rational basis; and is the only reasonable method by which California can require interstate commerce to pay its fair share of the marketing program costs.

**1. Non-Protectionist Purpose**

The California assessment scheme assesses interstate commerce for its fair share of the marketing program costs, and does not protect local industry from interstate competition. The mil assessment imposed against out-of-state processors is tied to the weight of processed beef

marketed in California, CFAC § 64713, and hence is *directly* proportionate to the benefits received from the marketing program. Further, California provides the benefits of its marketing program *equally* to the instate and out-of-state industries, and does not attempt to promote California beef at the expense of out-of-state beef. Finally, as noted earlier, the California industry pays a disproportionately heavier burden than the out-of-state industry to support the marketing program, because the California industry pays multiple fees for the same product and the out-of-state industry does not. See page 3, *supra*. These extrinsic factors make clear that the assessment scheme does not protect local industry. The Ninth Circuit, following its *per se* analysis, gave no weight whatsoever to these extrinsic factors, even though they rebut the Ninth Circuit's conclusion that the assessment scheme constitutes "simple economic protectionism." App. 7.

**2. Non-Discriminatory Effect.**

The California assessment scheme does not have a discriminatory effect under actual marketing conditions. As noted earlier, the Ninth Circuit acknowledged that the undisputed evidence shows that out-of-state processors "pass back" the mil assessments to out-of-state producers. App. 10; see pages 2-3, *supra*. Thus, the instate and out-of-state assessments are ultimately borne by producers who are in direct competition with each other. And, since the out-of-state assessments are *not* ultimately borne by out-of state processors, such processors sell in the market place on the same terms as local processors, and thus suffer no actual competitive disadvantage. The Ninth Circuit, following its *per se* analysis, dismissed these extrinsic factors as "legally insufficient" and "not controlling," App. 10-11, even though they rebut the Ninth Circuit's conclusion that the assessment scheme has a "discriminatory effect" and gives a "direct commercial advantage" to local business. App. 7.

Further, the undisputed evidence shows that the out-of-state mil assessments are *de minimus*—in that they are much less than the price differentials that affect actual retail purchasing decisions—and thus that the mil assessments would not cause an actual competitive disadvantage even if they were not passed back. Stip. 14. The Ninth Circuit made no reference to this extrinsic factor.

### 3. Rational Basis and Alternatives

As explained earlier, actual marketing conditions prevent California from imposing facially identical assessments against local and interstate commerce. See pages 2-3, *supra*. In particular, it is not possible to levy an assessment on out-of-state producers to correspond to the local head fee, because out-of-state producers cannot be identified after their product is marketed in California. *Id.* Faced with this dilemma, the California Legislature determined that the only fair and practical solution is to assess the single out-of-state group that can be readily identified, *i.e.*, processors who ship beef to California. The solution is particularly fair because out-of-state processors have the capacity to pass back the assessment to out-of-state producers, who compete with California producers who pay the local head fee. Indeed, as the district court below properly noted, California *has* achieved facial symmetry by imposing assessments against both the instate and out-of-state industries at the time of the *first sale* occurring when it is clear that the product will be marketed in California. App. 30.

The Ninth Circuit suggested an alternative scheme that would achieve facial symmetry but create substantial inequities that do not now exist. California, the court stated, could "shift" the instate assessments from producers to processors, and thus "tax" instate and out-of-state processors "equally." App. 15. This alternative, without more, would result in the loss of substantial revenues to support the marketing program, because California producers now

collectively pay two or three head fees for the same animal. Staiger Dec. 2; App. 32; Stip. 12. To overcome this problem, the Ninth Circuit suggested that the mil assessment "could be adjusted to compensate for the loss," App. 15, which apparently means either that (1) the suggested mil assessment on *California* processors could be raised to equal the two or three head fees now paid by California producers, or (2) the mil assessment on *both* instate and out-of-state processors could be raised to achieve the total revenue now obtained from the assessment scheme. Under the first possibility, California processors would pay substantially higher fees than out-of-state processors for the same product, and thus, paradoxically, would be the victims of facial discrimination. Under either possibility, the instate and out-of-state processors would pass back the assessments to their immediate suppliers, who would bear the entire brunt of the assessment program. Youde Dec. 2-8. The latter result would defeat the legislative goals of (1) spreading the marketing program costs across the entire industry, rather than focusing the costs on a single group of competitors, and (2) ensuring that no single competitor pays more than the equivalent of $1 per head of cattle. CFAC §§ 64691, 64713.

The Ninth Circuit's mechanical analysis thus leads to a thicket of practical and equitable problems that the Ninth Circuit obviously overlooked, and that the California Legislature wisely avoided. Because of actual marketing conditions in the beef cattle industry, it is simply infeasible to impose assessments "equally" on instate and out-of-state processors, contrary to the Ninth Circuit's assumption. Indeed, the Ninth Circuit alternative is even more drastic and inequitable than an alternative suggested by the plaintiffs below, which the Ninth Circuit apparently, and cor-

rectly, rejected for its obvious inequities.[8] California, which has responsibility for administering its marketing program under actual conditions, strongly believes that its legislative scheme is the only fair and practical means to require interstate commerce to pay its just share of the marketing program costs.

It is thus clear that the Ninth Circuit, by following a mechanical *per se* approach rather than considering the scheme in light of extrinsic circumstances, has departed from proper Commerce Clause analysis and reached the wrong result. The case thus raises significant federal questions worthy of plenary consideration.

## II

## THIS CASE RAISES SUBSTANTIAL FEDERAL QUESTIONS CONCERNING WHETHER A STATE MAY ASSESS INTERSTATE COMMERCE TO SUPPORT THE COSTS OF MARKETING PROGRAMS WHERE CONVENTIONAL "NEXUS" IS LACKING

In the proceedings below, the plaintiffs argued that California cannot impose assessments on out-of-state processors who do not have "nexus" with California,

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[8]The plaintiffs argued below that California should continue requiring California producers to pay the head fee, but in addition should impose a mil assessment on California processors. We responded that this alternative would be unfair to California producers because California processors would pass back the mil assessment to their immediate suppliers, who would then pay more than the equivalent of a single head fee. Moreover, by placing an additional fee on the California industry, the plaintiffs' suggested alternative would further increase the disproportionately heavy burden borne by the California industry. The Ninth Circuit, evidently agreeing with California's analysis, did not suggest this as a viable alternative.

whether or not the assessment scheme is discriminatory. The plaintiffs' nexus argument is based on this Court's decisions holding that states cannot *tax* out-of-state industries where sufficient "nexus" is lacking, and that nexus requires that the taxpayer have a "presence" in the taxing state. See, *e.g., Miller Bros. Co. v. Maryland,* 347 U.S. 340, 344-345 (1954); *National Bellas Hess, Inc. v. Illinois Dept. of Revenue, supra,* 386 U.S. at 756.

In California's view, the "nexus" requirement is necessarily satisfied—and in fact does not even apply—where a state imposes assessments for specific marketing benefits provided to interstate commerce. The conferring of the benefit entitles the state to impose an assessment whether or not the assessee has a "presence" in the state. This conclusion is supported by this Court's decisions upholding state "user" fees against interstate commerce—such as harbor fees, highway fees, and airport fees—where the fees compensate the state for specific services or facilities provided to interstate commerce. See, *e.g., Evansville-Vanderburgh Airport Authority Dist. v. Delta Airlines, Inc.,* 405 U.S. 707 (1972); *Clyde Mallory Lines v. Alabama,* 296 U.S. 261 (1935); *Capitol Greyhound Lines v. Brice,* 339 U.S. 542 (1950).

Concededly, the user fee cases are not wholly applicable here, because the assessee in each case was physically present in the assessing state and the conventional "nexus" requirement was therefore met. This fact, however, appeared to assume no significance in the decisions. Indeed, this Court has stated that nondiscriminatory state user fees are constitutionally sustainable if they are fairly apportioned and not excessive in relation to the costs of government, implying that conventional "nexus" is not required. See *Massachusetts v. United States,* 435 U.S. 444, 464 (1978). More directly, this Court has stated that:

> "[S]uch imposition, although termed a tax, cannot be tested by standards which generally determine the

validity of taxes." *Commonwealth Edison Co. v. Montana, supra,* 453 U.S. at 622 n. 12, quoting from *Interstate Transit, Inc. v. Lindsey,* 282 U.S. 183, 190 (1931).

In an analogous context, this Court has held that the federal government can impose fees against states for specific services or benefits provided by the federal government, notwithstanding the constitutional prohibition against federal taxation of states. See *Massachusetts v. United States,* 435 U.S. 444, 464 (1978). In *Massachusetts,* the Court stated:

> "[S]uch revenue measures by their very nature cannot possess the attributes that led Mr. Chief Justice Marshall to proclaim that the power to tax is the power to destroy. There is no danger that such measures will not be based on benefits conferred or that they will function as regulatory devices unduly burdening essential state activities." 435 U.S. at 460-461.

Similarly, state fees against interstate commerce, if based on specific benefits provided, by their very nature cannot enable the states to "unduly burden[ ]" such commerce.

The user fee cases appear to present a closer analogy here than the tax cases cited by the plaintiffs below, because the states in the user fee cases provided specific benefits to interstate commerce and the states in the tax cases did not. On balance, the Commerce Clause appears to pose no obstacle to state assessment schemes that legitimately compensate the state for specific benefits provided to interstate commerce, even where conventional "nexus" is lacking. Significantly, this Court has never undertaken to answer this important question, and the issue is one of the first impression.

The district court upheld California's nexus argument, ruling that the conferring of the benefit authorizes California to impose assessments on interstate commerce. App. 22-25. The Ninth Circuit expressly refrained from

reaching this question, on grounds that California's assessment scheme was invalid for other reasons. App. 4. The Ninth Circuit, however, impliedly upheld California's argument, declaring that California "probably confers a benefit on out-of-state beef processors and producers by encouraging the consumption of beef in California and, therefore, . . . the state may have a legitimate right to be compensated for rendering a beneficial service." App. 14.

Although the Ninth Circuit did not specifically decide the "nexus" issue, we request that this Court decide the issue if, on plenary consideration or otherwise, it reverses the Ninth Circuit decision on the discrimination issue. The "nexus" issue is related to the discrimination issue, because both involve application of the Commerce Clause to the same set of facts. The "nexus" issue was fully briefed by both parties before both lower courts, was specifically decided by one lower court and impliedly decided by the other, and involves purely legal issues rather than questions of fact. For these reasons, this Court should decide the "nexus" issue if it reverses on the discrimination issue, rather than remanding and inviting another proceeding here on the constitutional validity of the California assessment scheme.

## CONCLUSION

For the foregoing reasons, this Court should note probable jurisdiction and set the case for plenary consideration.

DATED: October 29, 1984

Respectfully submitted,

JOHN K. VAN DE KAMP
Attorney General of the
State of California
R. H. CONNETT
Assistant Attorney General
RODERICK E. WALSTON
Deputy Attorney General
(Counsel of Record)
ALLENE C. ZANGER
Deputy Attorney General
6000 State Building
350 McAllister Street
San Francisco, CA 94102
Telephone: (415) 557-3920
*Counsel for Appellants*

**(Appendices follow)**

## Appendix A

United States Court of Appeals

For the Ninth Circuit

No. 83-1979

D.C. No. CIV S-82-194 RAR

National Meat Association, American Meat Institute, et al.,
Plaintiffs-Appellants,

vs.

George Deukmejian, et al.,
Defendants-Appellees.

[Filed Sept. 21, 1984]

An Appeal From the United States District Court for the Eastern District of California, Hon. Raul A. Ramirez, Judge, Presiding, Argued and Submitted: February 16, 1984

OPINION

Before: MERRILL, FARRIS, and PREGERSON, Circuit Judges.

PREGERSON, Circuit Judge.

The National Meat Association, the American Meat Institute, and eleven beef processors appeal the district court's ruling upholding the constitutionality of a California tax on imported processed beef. We find that the California tax violates the Commerce Clause of the U. S. Constitution by discriminating against interstate commerce, and we reverse the district court's decision.

## I. FACTS

In 1956, the California Legislature enacted the California Beef Council Law, Cal. Agric. Code § 64501-64735 (West 1968). The purpose of the law was to promote the California beef industry. The statute described the beef industry as "a paramount industry of this state which not only provides substantial and required revenues for the state . . . and employment and means of livelihood for many thousands of its population, but also furnishes essential foods that are vital to the public health and welfare." Cal. Agric. Code § 64532 (West 1968).

The law created an advisory beef council of range cattlemen, cattlefeeders, and dairymen to conduct research and educational programs intended to expand the market for beef. Cal. Agric. Code § 64661 (West 1968). The law was later amended to add cattle slaughterers and one member of the general public to the Beef Council.

To stimulate demand for beef in California, the Council uses television and radio commercials, billboards, and posters. The council produces and distributes basic beef buying information, films, and school lesson plans regarding beef's role in a balanced diet, the beef industry's contribution to a healthy economy, and the importance of cattle in the economic and ecological systems. The Beef Council also studies consumer attitudes and market behavior to develop better advertising and educational programs.

Originally, the Beef Council was to be funded by voluntary contributions. In 1967, however, the law was amended to impose a mandatory ten cent "head fee" on all cattle sold in California. In 1978, the fee was increased to twenty-five cents per head.

In February 1982, the legislature once again amended the law in response to what it termed "[t]he current depressed conditions of the beef cattle industry, caused in part by consumer misconceptions regarding the role of red meat and animal fats in the basic diet . . . ." 1982 Cal. Legis. Serv. 94 (West). The amendment raised the head fee on cattle sold in California to $1.00 and, for the first time, imposed an assessment on out-of-state beef processors. This so called "mil assessment" taxed processors by the pound in boned, boxed, or carcass beef imported into California. The mil assessment charged to out-of-state beef processors is not the same as the in-state head fee. In-state fees are imposed on sellers of cattle—a flat per head charge. The out-of-state assessment is levied on a different group—beef processors. The assessment is made on a per pound basis and varies slightly with the type of processed beef.

In July 1982, the Beef Council law was further amended. The out-of-state assessment was reduced and restructured to insure that out-of-state processors would not be charged more than the equivalent of the $1.00 head fee imposed on California beef producers.

In March 1982, two nationwide associations of beef processors and eleven individual out-of-state beef processors brought the instant suit. The processors contended that the California Beef Council law violates the Commerce Clause of the United States Constitution, (art. I, § 8, cl. 3) by discriminating against interstate commerce and violates both the Commerce Clause and Due Process clauses (amend. XIV, § 1) by imposing a tax on beef processors who lack

sufficient contacts or "nexus" with California and, therefore, are outside the reach of the state's taxing power.[1]

At pretrial conference, the parties to this suit stipulated that there were no triable issues of fact and agreed to submit the case on cross-motions for summary judgment. The district court granted summary judgment in favor of the state defendants, which we now reverse.

Because we hold that the California tax discriminates against interstate commerce, we do not reach the nexus issue.[2] *See Armco Inc. v. Hardesty*, 52 U.S.L.W. 4787 (U.S. June 12, 1984) (Supreme Court does not reach nexus issue

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[1]Nexus "is the outstanding prerequisite on state power to tax. Consistent with this requirement there must be 'some definite link, some minimum connection, between the state and the person, property or transaction it seeks to tax.' " *American Oil Co. v. Neill*, 380 U.S. 451, 458 (1965) (quoting *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344-45 (1954)). The importance of nexus as a prerequisite for the taxation of interstate commerce was reaffirmed in *Complete Auto Transit v. Brady*, 430 U.S. 274, 285 (1977), and *Maryland v. Louisiana*, 451 U.S. 725, 754 (1981). *See National Geographic Soc'y v. Board of Equalization*, 430 U.S. 551 (1977) (allowing state to impose duty to collect tax on out-of-state corporation that maintained advertising offices in state), *National Bellas Hess v. Dept. of Revenue*, 386 U.S. 753 (1967) (striking down state tax on out-of-state mail order firm that maintained no offices or representatives in taxing state).

[2]We also do not reach an issue raised by the Meat Importers Council of America, filing as *amicus curiae*. They contend that a California assessment on imported beef is unconstitutional under the Commerce Clause, U.S. Const. art. I, § 8, cl. 3 (granting Congress the authority to regulate commerce with foreign nations), and the Import-Export Clause, U.S. Const. art. I, § 10, cl. 2 (providing that "[n]o state shall, without the consent of Congress, lay any Impost or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws."). We note that this issue was not litigated in the district court, and we do not decide it on this appeal.

because it found West Virginia tax unconstitutionally discriminated against interstate commerce).

## II. STANDARD OF REVIEW

Grants of summary judgment are reviewable by this court de novo. *National Union Fire Insurance Co. v. Argonaut Insurance Co.*, 701 F.2d 95, 96 (9th Cir. 1983). Summary judgment is properly granted when it appears that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c). Here, because the parties stipulated to all material facts, we are concerned only with matters of law.

## III. LEVEL OF SCRUTINY

We consider the issue of discrimination against interstate commerce raised in this case in light of the balance that must be maintained between the purpose of the Commerce Clause, " 'to create an area of free trade among the several states,' " *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 328 (1977) (quoting *McCleod v. J. E. Dilworth Co.*, 322 U.S. 327, 330 (1944)), and "the legitimate interest of the individual States in exercising their taxing powers . . . ." *Boston Stock Exchange*, 429 U.S. at 329. We note that this balancing of interests requires careful analysis of the facts of each individual case.

> [T]he delicate balancing of the national interest in free and open trade and a State's interest in exercising its taxing powers requires a case-by-case analysis and . . . such analysis has left " 'much room for controversy and confusion and little in the way of precise guides to the States in the exercise of their indispensable power of taxation.' "

*Westinghouse Electric Corp. v. Tully*, 52 U.S.L.W. 4485, 4489 (U.S. April 24, 1984) (quoting *Boston Stock Exchange*, 429 U.S. at 329, which quotes *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 457 (1959)). Thus, every commerce clause challenge turns upon the specific facts presented.

We also appreciate the distribution established by the Supreme Court between "protectionist" measures employed by states to favor local businesses and measures employed by states to safeguard the health and safety of their people. While the latter may be upheld if treatment of intrastate and interstate commerce is evenhanded and if effects on interstate commerce are only incidental, the former are subject to a "virtually per se rule of invalidity . . . ." *Philadelphia v. New Jersey*, 437 U.S. 617, 623-24 (1978) (invalidating a New Jersey statute prohibiting importation of solid or liquid waste originating outside the state). *See Minnesota v. Clover Leaf Creamery*, 449 U.S. 456, 471-72 (1981) (upholding Minnesota statute banning retail sale of milk in plastic non-returnable containers); *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970) ("Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits.").

"A finding that state legislation constitutes 'economic protectionism' may be made on the basis of either discriminatory purpose or discriminatory effect." *Bacchus Imports v. Dias*, 52 U.S.L.W. 4979, 4981 (U.S. June 29, 1984) (citations omitted). In the instant case, the California beef

tax on out-of-state processors has a discriminatory effect; therefore, there is no need for us to address the issue of discriminatory purpose. Because we find discriminatory effect, the California beef tax at issue constitutes economic protectionism. Thus, we apply a very strict level of scrutiny—a "virtually per se rule of invalidity."

## IV. DISCRIMINATORY EFFECT

The California beef tax is discriminatory on its face. Out-of-state beef processors are taxed according to the quantity of beef they market in California, while no comparable tax is levied on in-state beef processors. Facial discrimination, however, is not the decisive factor. As the Supreme Court stated in *Maryland v. Louisiana*, 451 U.S. 725, 756 (1981):

> A state tax must be assessed in light of its actual effect considered in conjunction with other provisions of the State's tax scheme. "In each case it is our duty to determine whether the statute under attack, whatever its name may be, will in its practical operation work discrimination against interstate commerce."

541 U.S. at 756 (quoting *Best & Co. v. Maxwell*, 311 U.S. 454, 455-56 (1940)).

Examining the assessment imposed on out-of-state beef processors "in light of its actual effect" and considering it in conjunction with assessments on the in-state beef industry, we conclude that the assessment discriminates against interstate commerce in practical operation because (1) it treats out-of-state taxpayers differently from similarly situated in-state taxpayers, and (2) it gives a direct commercial advantage to local business. Both points are discussed below.

### A. *Unequal Treatment*

*Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 70 (1963) laid down the rule requiring equal treatment of similarly situated in-state and out-of-state taxpayers. In *Halliburton*, the Supreme Court invalidated a Louisiana use tax that treated similarly situated taxpayers differently. The Court observed that "equal treatment for in-state and out-of-state taxpayers similarly situated" is a condition precedent to validity under the Commerce Clause. *Id.* at 70. The appellant in *Halliburton* manufactured special equipment in Oklahoma for use in its Louisiana operations. Because the equipment was manufactured outside Louisiana, the appellant was charged a use tax on the full value of the assembled equipment. A similarly situated business both manufacturing and using the equipment in Louisiana paid tax on the value of the raw materials only. The Louisiana tax placed the out-of-state manufacturer-user on the same footing as an in-state competitor who chose to buy special equipment in Louisiana at retail, but not with an identically situated in-state competitor, who manufactured its own special equipment.

Here, the California beef assessment violates the *Halliburton* rule of equal treatment. Out-of-state beef processors are taxed; their California counterparts are not. The structure of the assessment requires different treatment of identically situated in-state and out-of-state taxpayers.

### B. *Direct Advantage to Local Business*

By taxing out-of-state beef processors and not taxing their in-state competitors, California gives a direct commercial advantage to local business. The Supreme Court has repeatedly held that the Commerce Clause forbids

such preferential treatment. In *Bacchus Imports v. Dias*, 52 U.S.L.W. 4979 (U.S. June 29, 1984) the Supreme Court invalidated Hawaii's excise tax on sales of wholesale liquor that exempted several kinds of locally produced wines and spirits. Hawaii defended the facially discriminatory exemptions by arguing that they were a reasonable means of promoting the consumption of liquors made from indigenous Hawaiian plants. The Supreme Court rejected the state's justification for the discriminatory exemption and held that it is "a cardinal rule" that "[n]o State, consistent with the Commerce Clause, 'may impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business.'" 52 U.S. L.W. at 4981 (quoting *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 329 (1977). *See also Maryland v. Louisiana*, 451 U.S. 725 (1981) (invalidating Louisiana's "first-use" tax on natural gas because, *inter alia*, in-state users were favored by a series of exemptions and credits); *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318 (1977) (invalidating a New York stock transfer tax scheme because it reduced the tax payable by non-residents when the transfer involved an in-state sale, and also set a maximum limit to the tax payable on an in-state, but not on an out-of-state, sale).

Here, as in *Bacchus*, the state argues that the discriminatory assessment is a reasonable means of promoting the consumption of beef. But the means chosen to promote the consumption of beef provide a direct commercial advantage to California beef processors by levying a tax on their out-of-state competitors. The Commerce Clause forbids such preferential treatment.

### C. *Passback Theory*

Despite clear differential treatment of interstate and intrastate commerce, the district court concluded that the California tax was non-discriminatory. The district court's holding was based on the testimony of the state's economic expert who expressed the view that the tax on out-of-state beef processors would not be discriminatory in practical effect because those beef processors would be able to shift the tax burden to out-of-state beef producers. If this assertion is true, identically situated taxpayers, in-state and out-of-state beef producers, would shoulder the burden of the tax, and identically situated in-state and out-of-state processors would be free of it.

The state's argument that the tax imposed on out-of-state beef processors will be "passed back" to out-of-state producers is based on an analysis of present economic conditions in the cattle industry. According to Dr. James G. Youde, an expert agricultural economist who testified for the state, the "pass back" takes place because meat processors have an "economic edge" over cattle feeders and ranchers. Dr. Youde ascribes this edge to significant expansion of United States beef cattle supplies over the past twenty years.

The appellant meat associations submitted no evidence to counter the state's economic testimony. Nonetheless, we have concluded that this testimony is not controlling. In *Armco Inc. v. Hardesty*, 52 U.S.L.W. 4787, 4789 n.8 (U.S. June 12, 1984), the Supreme Court held that a state tax could not be upheld on the basis of economic factors that might somehow mitigate its direct burden on interstate commerce.

> Courts are not possessed of instruments of determination so delicate as to enable them to weigh the various factors in a complicated economic setting which, as to the isolated application of the State tax, might mitigate the obvious burden generally created by a direct tax on commerce.

*Freeman v. Hewit*, 329 U.S. 249, 256 (1946) (quoted in *Armco*, 52 U.S.L.W. at 4789 n.8).[3]

Thus, any existing economic setting in the beef cattle industry, which may theoretically allow out-of-state processors to pass back California's tax to out-of-state beef producers, is legally insufficient to overcome the burden imposed on interstate commerce by California's taxing scheme.

D. *Compensatory Tax Theory*

The state argues that even if we do not accept the pass-back theory, the assessment on out-of-state beef processors can be justified as a compensatory tax, i.e., one that would complement assessments on in-state beef producers. The

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[3]Our conclusion is supported by the Supreme Court's decision in Bacchus Imports, Ltd., ..... U.S. ....., 104 S.Ct. 3049, 3054 (1984). In *Bacchus Imports*, the state argued that liquor wholesalers lacked standing to attack the constitutionality of a discriminatory tax because they could shift the burden of the tax to their customers. The Supreme Court found that the cost-shifting theory did not affect the wholesaler's standing—(1) expressing doubt that wholesalers could actually pass on the tax, and (2) finding standing even if the burden could be shifted.

Further, we are not aware of any decision in which a discriminatory tax has been upheld on the ground that the payor had the ability to shift the incident of the tax. Such a holding would permit a state to discriminate against any out-of-state seller who was powerful enough to extract favorable concessions from its suppliers. Moreover, the constitutionality of such a scheme could fluctuate as a function of market conditions.

Supreme Court has upheld apparently discriminatory tax treatment when the tax on interstate commerce complemented an in-state tax, designed to equalize the in-state and out-of-state tax burden and to make interstate commerce pay a just share of state taxes.

The most common example of such a taxing scheme is an in-state sales tax and compensatory use tax on goods imported from out-of-state. First sanctioned by the Supreme Court in *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937), sales and use tax schemes act to equalize the in-state and out-of-state tax burden. As the Supreme Court reiterated in *Halliburton:*

> "Equality is the theme that runs through all the sections of the statute. . . . No one who uses property in Washington after buying it at retail is to be exempt from a tax upon the privilege of enjoyment except to the extent he has paid a use or sales tax somewhere." The use tax is "upon one activity or incident," and the sales tax is "upon another, but the sum is the same when the reckoning is closed." The burden on the out-of-state acquisition "is balanced by an equal burden where the sale is strictly local."

373 U.S. at 70 (quoting *Henneford*, 300 U.S. at 583-84).

In presenting California's tax on out-of-state beef processors as a compensatory tax, the state relies on *Alaska v. Arctic Maid*, 366 U.S. 199 (1961). In *Arctic Maid*, the Supreme Court upheld the validity of an Alaskan tax on freezer ships that froze salmon caught in Alaskan waters for transport to out-of-state canneries. The freezer ship owners argued unsuccessfully that there was no equivalent tax on local freezing operations. In fact, there was a complementary local tax, levied not against businesses who

froze fish for the fresh fish market, but against local canners. Although out-of-state freezer ships were being treated differently from local freezers, they were taxed less than local canners, who, although technically engaged in another business, were the freezer ships' closest competitors.

The state contends that *Arctic Maid* allows states to impose compensatory taxes on interstate commerce so long as the effect of the total tax scheme does not impose a greater burden on interstate commerce than on intrastate commerce. *Arctic Maid* is distinguishable from the instant case. A key factor prompting the Supreme Court to uphold the tax in *Arctic Maid* was that while the out-of-state compensatory tax was directed at a business different from the business subject to the in-state tax, the different businesses were direct competitors. The out-of-state business was not placed at a competitive disadvantage, because its closest in-state competitor was also taxed.

In this case, the different businesses being taxed are not competitors. The tax on out-of-state beef processors is not balanced by a tax on their in-state competitors. Thus, unlike the situation in *Arctic Maid*, the out-of-state taxpayer here is discriminated against vis-a-vis its local counterpart.

## V. COMPENSATING CALIFORNIA FOR BENEFITS CONFERRED

Our decision today is not intended to infringe on the legitimate power of the states to tax interstate commerce in order to obtain fair compensation for state services. We recognize that states are entitled to make interstate commerce pay its fair share for beneficial state services. "The Commerce Clause balance tips against the tax only when it unfairly burdens commerce by exacting more than a just

share from the interstate activity." *Washington Rev. Dept. v. Stevedoring Ass'n.*, 435 U.S. 734, 748 (1978). As Justice Frankfurter noted, "[t]he simple but controlling question is whether the state has given anything for which it can ask return." *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940).

We recognize that the California Beef Advisory Council probably confers a benefit on out-of-state beef processors and producers by encouraging the consumption of beef in California and, therefore, that the state may have a legitimate right to be compensated for rendering a beneficial service.[4] We cannot, however, accept California's discriminatory taxing scheme as the means by which such compensation may be realized. There are non-discriminatory means available. In *Dean Milk Co. v. City of Madison*, 340 U.S. 349 (1951), the Supreme Court struck down local regulations restricting the importation of milk because the health-oriented purpose could have been achieved by less discriminatory means. The Supreme Court said:

> In thus erecting an economic barrier protecting a major local industry against competition from without the State, Madison plainly discriminates against interstate commerce. This it cannot do, even in the exercise of its unquestioned power to protect the health and safety of its people, if reasonable nondiscriminatory

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[4]Parties stipulated that approximately 60% of beef consumed in California is produced in other states. After the 1982 amendments, combined Beef Council assessments are expected to total 5.3 million dollars annually of which only 2.1 million dollars, or 40%, will be in the form of mil assessments, the type of assessment levied on out-of-state processors. Therefore, the out-of-state beef industry would have paid substantially less and theoretically benefitted substantially more from the California Beef Council promotions than the in-state beef industry.

> alternatives, adequate to conserve legitimate local interests, are available.

340 U.S. at 354 (footnote omitted).

The state argues that its discriminatory means are justified. The state explains that it is impossible to levy a head fee against an out-of-state cattle producer at the time of an out-of-state sale because it is unknown whether the beef will ever be marketed in California.[5] The beef processors, who actually ship beef into California, are the parties in the production chain with whom California first has sufficient nexus to tax. Likewise, in California, the earliest practical time to assess a fee is at the time of sale or slaughter. Assessing a head fee on live cattle at the time of sale is administratively simpler and, if a fee is assessed every time an animal is sold, the potential for more revenue exists.

Without passing on the validity of any alternate tax scheme, we note that non-discriminatory means of financing the Beef Council appear to be available. For example, California could shift the in-state assessment from cattle producers to beef processors and tax in-state and out-of-state beef processors equally. We recognize that this change would eliminate multiple taxes potentially available on a single animal because a head fee is charged everytime a sale occurs. But the assessment could be adjusted to compensate for this loss. In short, it appears that less discriminatory means appear to be available.

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[5]California would, of course, have no constitutional basis for taxing beef raised and consumed outside of California because the required nexus would be lacking. See footnote 1, *supra*.

## VI. CONCLUSION

In light of recent Supreme Court Commerce Clause precedent, *e.g., Bacchus Imports v. Dias,* 52 U.S.L.W. 4979 (U.S. June 29, 1984); *Armco Inc. v. Hardesty,* 52 U.S.L.W. 4787 (U.S. June 12, 1984), the California assessment on imported processed beef cannot stand. Its clearly discriminatory treatment of interstate commerce cannot be excused by evidence of economic factors that might mitigate the direct burden on interstate commerce, nor can the tax be justified when other less discriminatory means exist. The judgment of the district court is REVERSED.

562 F.Supp. 357 (1983)

In the United States District Court
For the Eastern District of California

No. CIV.S-82-194 RAR

National Meat Association, et al.,
Plaintiffs,

v.

George Deukmejian, Governor of California, et al.,
Defendants.

[Filed April 21, 1983]

## MEMORANDUM AND ORDER

At issue in this case is the constitutionality of the 1982 amendments to the California Beef Council Law, Cal. Food & Ag. Code § 64501, *et seq.* (West, 1967),[1] which required for the first time that out-of-state beef processors as well as in-state cattlemen support the California Beef Council. In March of 1982, plaintiffs, two nationwide associations of beef processors and eleven individual out-of-state beef processors,[2] brought suit seeking declaratory and injunctive relief for alleged violations of the Commerce Clause and

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[1]Unless specially indicated, all subsequent citations are to the California Food and Agriculture Code.

[2]In May of 1982, pursuant to stipulation of counsel, another individual out-of-state beef processor was added as party plaintiff. On September 13, 1982, the Court granted the motion of Harris Farms, et al., individual in-state beef processor, for leave to participate as *amici curiae*.

the Equal Protection Clause.[3] Upon completion of discovery, both parties moved for summary judgment, F.R.Civ.P. 56.

The cross-motions of the respective parties came on specially for hearing before the undersigned on February 7, 1983. Hershel Shanks, Esq., of Glassie, Pewett, Dudley, Beebe & Shanks, appeared on behalf of plaintiffs; Roderick Walston, Deputy Attorney General, appeared on behalf of defendant; John Foote, Esq., of Thelen, Marrin, Johnson & Bridges, appeared on behalf of *amici curiae*. Having carefully reflected upon the arguments of opposing counsel presented in their briefs and at oral argument, the Court hereby issues the following Memorandum and Order:

Subject matter jurisdiction is predicated upon the basis of federal question, 28 U.S.C. § 1331. As correctly stipulated by the parties, disposition of the case by summary judgment is appropriate, the issue being one of law and there being no material facts in dispute.

Turning to the merits of the case, the Court hereby grants defendants' cross-motion for summary judgment holding that the 1982 amendments are constitutional for the reasons as set forth below.

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[3]Although the complaint also alleged violations of the Contract Clause and the Due Process Clause, those allegations do not warrant separate treatment at this time. The Contract Clause claim, as plaintiffs' counsel conceded at oral argument, has been abandoned. The Due Process claim, as conceded in plaintiffs' brief, pp. 22-24, is subsumed under the Commerce Clause claim.

## I. THE STATUTORY SCHEME

In 1956 the California Legislature enacted the California Beef Council Law (CBCL) for the stated purpose of promoting consumption of beef. Responsibility for the statute's enforcement was vested in the Beef Council Director, § 64562, who was to be assisted by an advisory body called the California Beef Council. § 64591. The Director was charged with carrying out education, research, public information and advertising programs designed to increase the consumption of beef.[4] The statute provided that the Director's activities were to be funded solely by "head fees", fees imposed each time a head of cattle was sold or slaughtered. Although payment of the head fee was originally voluntary, in 1967 the California Legislature made payment of the fee mandatory. In 1978 the fee was increased from $0.10 per head to $0.25 per head. § 64691.

In 1982, the California Legislature passed two bills, A.B. 960 and A.B. 2631, which substantially amended the CBCL. The first bill, A.B. 960, was enacted on February 1, 1982 as an urgency statute in response to the "depressed conditions of the beef cattle industry, caused in part by consumer misconceptions regarding the role of red meat and animal fats in a basic diet". A.B. 960 § 10. The new law raised the head fee on California cattle from $0.25 to $1.00 per head and imposed, for the first time, mandatory assessments on out-of-state beef processors. An out-of-state beef processor was defined as the "last person, firm, or corporation who slaughters or otherwise processes beef which is shipped into

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[4]For a detailed description of the activities of the California Beef Council, see the Statement of Ms. Jane Anderson, Executive Manager of the California Beef Council.

the state". § 64711. Section 64713 distinguished between chilled carcass, boxed beef, and boned beef,[5] and imposed thereon a per-pound assessment of $0.00200, $0.00233, and $0,00323, respectively.

A.B. 2631, enacted on July 2, 1982, further amended the CBCL reducing by twenty-five percent (25%) the per pound assessments, called "mil assessments," on all out-of-state processed beef. As a result of A.B. 2631, the mil assessment on chilled carcass was reduced to $0.00150, on boxed beef to $0.00175, and on boned beef to $0.00242. It further provided that:

> [out-of-state beef processors] shall not be required to pay an amount in excess of the equivalent of one dollar ($1) per head. Any person who pays an assessment in excess of the equivalent of one dollar ($1) per head shall be entitled to a refund of the excess portion of the payment so long as the person demonstrates to the satisfaction of the director or his or her agent that a refund is warranted. The assessment provided in this section is intended to be the equivalent of the [head] fee provided in Section 64691.

Section 64713.

## II. QUESTIONS PRESENTED

Plaintiffs contend that the mil assessments violates the Commerce Clause in two respects: first, there is an insufficient nexus between California and either the taxed activity (importation of processed beef) or the taxpayer

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[5]These are terms of art within the beef industry. For example, Section 64712.5 defines "boxed beef" as "beef that is broken down or cut into primal and subprimal cuts, vacuum sealed in a barrier bag and placed in a shipping carton for shipment to a customer".

(the out-of-state beef processor); second, the assessments discriminate against interstate commerce by imposing the fees on out-of-state beef processors but not on in-state beef processors and by charging an amount which in many instances exceeds the $1 head fee imposed on California cattle. Plaintiffs also argue that the composition of the California Beef Council violates the Equal Protection Clause inasmuch as out-of-state beef processors are irrationally and unjustifiably deprived of representation on that body. The Commerce Clause and Equal Protection Clause issues are addressed in turn.

## III. THE ASSESSMENTS DO NOT VIOLATE THE COMMERCE CLAUSE[6]

In deciding the merits of the Commerce Clause issues, the Court pays special heed to the caveat laid down by the Supreme Court:

> [w]hen called upon to make the delicate adjustment between the national interest in free and open trade and the legitimate interest of the individual States in exercising their taxing powers, the Court has counseled that the result turns on the unique characteristics of the statute at issue and the particular circumstances in each case.

*Boston Stock Exch. v. State Tax Com'n*, 429 U.S. 318, 329 (1977). This caveat has special application to the instant litigation because the special circumstances of this case set it apart from many of its precedents. Thus, rather than mechanistically conforming to prior results, this Court en-

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[6]The Commerce Clause provides that "Congress shall have Power . . . [t]o regulate Commerce . . . among the several States". Art. I § 8, cl. 3.

deavors to reach a decision consonant with both principles by taking full account of the unique characteristics of the statute at issue.

The most closely applicable standard by which the California statute must be measured is the one set forth in *Complete Auto Transit Inc. v. Brady*, 430 U.S. 274 (1977). In *Brady*, the court declared that a general state revenue tax is consistent with the Commerce Clause if it:

> is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State.

*Id.* at 279. Implicitly conceding that the California scheme is fairly apportioned and related to state-provided services, plaintiffs limit their attack to the other two prongs—the nexus and discrimination tests.

### (a) *The Nexus Prong*

Plaintiffs argue that the California law fails the nexus test because it applies to plaintiffs which do not have a physical presence within the State of California.[7] In support of this proposition, plaintiffs cite two sales/use tax cases where the Supreme Court ruled unconstitutional state efforts to require out-of-state sellers to collect use taxes imposed on their own residents. *National Bellas Hess v. Dept. of Rev.*, 386 U.S. 753 (1967); *Miller Bros. v. Maryland*, 347 U.S. 340 (1954). In *Bellas Hess* the only contacts between the Missouri mail order house and the State of

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[7]The parties have stipulated that eight plaintiffs have sufficient contacts with California for nexus purposes. However, plaintiffs contend that several do not. They cite as examples plaintiffs Litvak, National and Pepper which do nothing more than solicit orders by telephone and then ship beef by common carrier into California.

Illinois were via the U.S. mails. In *Miller Bros.*, the Delaware department store's contacts with Maryland took the form of general advertising and occasional truck deliveries. In both cases, the court found these contacts insufficient to meet the nexus test.

From these cases, plaintiffs derive a "physical presence" test which this Court refuses to adopt. Nowhere in these opinions is to be found a crude "physical presence" test. As the Supreme Court recently made clear, the nexus test is of quite a different character:

> [t]he relevant constitutional test to establish the requisite nexus for requiring an out-of-state seller to collect and pay the use tax is . . . simply whether the facts demonstrate "some definite link, some minimum connection, between [the state and] the person . . . it seeks to tax".

*National Geo. Soc. v. Cal. Bd. of Equal.*, 430 U.S. 551, 562 (1977), *citing Miller Bros., supra,* at 344-45. Even *Miller Bros.* envisioned the possibility that a state could, consistent with the Commerce Clause, extend its taxing power extraterritorially:

> [V]isible territorial boundaries do not always establish the limits of a state's power or jurisdiction . . . If there is some jurisdictional fact or event to serve as a conductor, the reach of a state's taxing power may be carried to objects of taxation beyond its border.

*Miller Bros., supra,* at 537-38. Other cases have used different phrases to express the same concept. *Wisconsin v. J. C. Penney,* 311 U.S. 435, 444 (1940), declares "the simple but controlling question is whether the state has given anything

for which it can ask return". *Michelin Tire Corp. v. Wages,* 423 U.S. 276, 288 (1976), speaks of taxation as the *quid pro quo* for benefits actually conferred by the taxing state.

Embodied in all these formulations is the idea that the nexus requirement serves the purpose of assuring that only those taxpayers who receive benefits from the state are subject to its taxing power. In the context of a general revenue tax, such as a sales or use tax, the benefits conferred are those of "police and fire protection, the benefit of a trained workforce, and the 'advantages of a civilized society' ". *Commonwealth Edison v. Montana,* 345 U.S. 609, 625 (1981), citing *Exxon Corp. v. Wisconsin Dept. of Rev.,* 447 U.S. 207, 228 (1980), quoting *Japan Line Ltd. v. City of Los Angeles,* 441 U.S. 434, 445 (1979). Because only those who are physically present within a state benefit from general government services, it is axiomatic that the state's taxing power is limited accordingly.

The facts presented by the case at bar are of quite a different order. Here the benefits received are not limited to the "advantages of a civilized society". On the contrary, the plaintiff out-of-state beef processors directly benefit from programs which are specifically tailored to promoting their product.[8] In other words, the benefit which plaintiffs receive is the intangible but nonetheless substantial benefit of increased revenues, not the geographically limited benefit of general governmental services.

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[8]Plaintiffs have stipulated to the fact that out-of-state beef processors benefit from the California Beef Council's programs. (Stip. #27). Moreover, the benefit must be substantial; each of the plaintiffs ship a minimum of $5 million pounds of beef into California each year. (Stip. #39).

In this Court's view, the combination of direct receipt of benefits from a program specifically catering to plaintiffs' interests and plaintiffs' affirmative conduct in sending beef into the California market constitute the "affirmative link[s]" which the nexus test requires.[9]

(b) *The Discrimination Prong*

Discriminatory taxes, plaintiffs correctly contend, violate the Commerce Clause:

> One of the fundamental principles of the Commerce Clause jurisprudence is that no State, consistent with the Commerce Clause, may "impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business". *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 458 (1959).

*Maryland v. Louisiana, supra,* at 754. Moreover, it is this Court's duty "to determine whether the statute under attack, whatever its name may be, will in its practical operation, work discrimination against commerce." *Id.* at

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[9]The court notes that because the nexus test embodies the minimum contacts test of the Due Process Clause, it finds an analogy to the exercise of long-arm jurisdiction useful. Just as less in the way of a physical presence by the defendant is required when the defendant's activities are related to the subject-matter of the lawsuit than when they are not, so too it is reasonable to require less in the way of a physical presence when the taxpayer receives benefits directly related to the taxpayer's conduct than when the taxpayer only receives general services.

In light of the ruling that the combination of direct receipt of benefits and beef shipment into California satisfies the nexus requirement, the Court finds it unnecessary to rule on plaintiffs' argument that the handler provisions, § 64710, *et seq.*, violate the Due Process Clause.

756. On the other hand, so long as the tax burden on interstate commerce is no greater than on intrastate commerce, the tax may be upheld as nondiscriminatory. *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937). When two purportedly complementary taxes are at issue, the Court must evaluate the effect of the tax scheme as a whole. If the tax on interstate commerce fairly compensates for a tax on local commerce, it is consistent with the Commerce Clause. *Alaska v. Artic Maid*, 366 U.S. 199 (1961). With these principles in mind, the Court examines the California statute.

The circumstances surrounding the passage of the subject legislation demonstrates that the legislation was passed for the non-discriminatory purpose of increasing beef consumption, as opposed to the impermissible purpose of giving a competitive edge to the California cattle industry. At the same time that California imposed the assessment burden on out-of-state beef processors it increased fourfold the burden on the California industry. In July, apparently concerned that the mil assessments might result in out-of-state beef processors shouldering a disproportionate burden, the legislature reduced the mil assessment by twenty-five percent (25%) and expressly provided that out-of-state beef processors shall not be required to pay an amount in excess of the equivalent of one dollar ($1.00) per head. The legislature chose not to reduce similarly the burden on the California industry.

The foregoing circumstances leave no room for doubt concerning California's intentions in regard to the 1982 amendments to the California Beef Council Law. California clearly intends that the mil assessments be equivalent to

the head fees and that out-of-state beef processors pay no more than their fair share of the Beef Council's programs.

The absence of a discriminatory intent sets the California scheme apart from several cases on which plaintiffs strongly rely. *Halliburton Oil Well Cementing Co. v. Reily,* 373 U.S. 64 (1963), overturned Louisiana's sales/use tax scheme because it was found to have been enacted for the purpose of (and with the effect of) favoring local users over out-of-state users similarly situated. New York's tax on the transfer of securities which had the purpose and the effect of channeling sales of securities into New York was struck down in *Boston Stock Exch. v. State Tax Com'n,* 429 U.S. 319 (1977).

Because the Court finds that the 1982 amendments were enacted for a non-discriminatory purpose, their only possible constitutional flaw arises from the amendments' effect on interstate commerce. Plaintiffs' first argument is that the statute discriminates against out-of-state beef processors by taxing them, but not their competitors, the in-state beef processors. This, plaintiffs argue, violates the principle of "equal treatment for in-state and out-of-state taxpayers similarly situated". *Halliburton Oil, supra,* at 70. In other words, plaintiffs would have this Court rule that because the statute treats dissimilarly entities on the same level of the distribution chain, it is discriminatory. This reasoning, because it ignores two important qualifying principles, is rejected as overly simplistic.

First, the duty of this Court is to evaluate the statute in terms of its practical effect, not its formal structure, *Complete Auto, supra,* at 279. The mere fact that the structure of the statute is such that the taxes are imposed

on different levels of the distribution chain does not render the statute unconstitutional. *Henneford, supra,* (upheld Washington's sales/use tax scheme which imposed a use tax on consumers and a sales tax on sellers); *Arctic Maid, supra,* (upheld Alaska's tax on fishing vessels which was deemed complementary to its tax on local canneries). Instead, the statute may be struck down only if its practical effect is to give without justification, a competitive advantage to in-state processors.[10]

In the present case, the evidence demonstrates that out-of-state processors are on a par with their in-state competitors. Indeed, defendants have filed expert affidavits which indicate that out-of-state beef processors will not suffer an economic disadvantage relative to California beef processors.[11] This conclusion is derived from the fact that beef processors have greater market power than entities higher up the distribution chain and therefore out-of-state beef processors are capable of passing-back the assessment to entities higher up on the chain.

Plaintiffs have presented no rebuttal evidence to the expert affidavits presented by the defendants. Instead, plaintiffs argue that the laws of supply and demand preclude

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[10]Plaintiffs contend that having established that on its face the statute discriminates between in-state and out-of-state beef processors, the burden of proof shifts to defendants (Plaintiffs' Opening Brief, p. 39). This contention is rejected because it is contrary to the general rule that the burden of proof falls on plaintiffs, *Norton Co. v. Dept. of Rev.*, 340 U.S. 534, 537 (1951), and plaintiffs have failed to cite any authority for the proposition that an exception exists in this type of case.

[11]Declaration of Dr. James Youde, p. 2, ¶ 6, Defs.' Exh. #9; Declaration of Mr. Philip Bauer, p. 1, ¶ 6, Defs.' Exh. #10.

the cost shifting as described.[12] Accordingly, this Court believes that the preponderance of the evidence supports defendants' position and finds as a matter of fact that out-of-state beef processors are not economically disadvantaged *vis-a-vis* in-state beef processors by virtue of the mil assessments.

Still another ground exists for rejecting plaintiffs' argument: the *Halliburton* equality principle explicitly recognizes that deviations from strict equality are constitutionally acceptable if adequately justified, as is true here.

*Halliburton* did not erect a *per se* rule against differing treatment of similarly situated taxpayers. Rather, it concluded that:

> the proper comparison on the basis of this record is between in-state and out-of-state manufacturer-users. And if this comparison discloses discriminatory effects, it would be ignored only by a *showing of adequate justification.*

*Id.*, at 71 (emphasis added). Thus a statute which treats similarly situated taxpayers differently may nonetheless pass constitutional muster if the different treatment is adequately justified.

On the record now before the Court, the Court finds that the disparate treatment alleged by the plaintiffs is adequately justified. As to both California cattle and out-of-

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[12]Plaintiffs do not present evidence tending to show that the fees will not be *passed on* to consumers. Committee Statement on A.B. 960; Letter from Mr. William Staiger to Gov. Edmund Brown, Jr., dated January 22, 1982; Letter from Mr. George Strathearn to Gov. Edmund Brown, Jr., dated January 26, 1982. However, plaintiffs' evidence against a "pass-on" does not undermine defendant's evidence of a "pass-back."

state cattle ultimately consumed in California, the tax is levied at the earliest feasible point in time. The earliest practicable point for California cattle to be assessed is at the time of sale or slaughter. The earliest practicable point for out-of-state cattle to be assessed is at the time of entry into the state. Prior to entry, it is impossible to predict the ultimate destination of the non-California cattle. (Stip. #38). Moreover, it is reasonable to impose mil assessments on processed beef and head fees on live cattle. Head fees are wholly impracticable for processed beef because beef is typically commingled at the slaughterhouse and the identity of the original producer cannot be traced. (Stip. #14). Likewise, assessing a head fee on live cattle is an administratively simpler means of generating revenue than mil assessments.

Having rejected plaintiffs' argument that the statute is unconstitutional because it places a tax burden on out-of-state beef processors, the Court now turns to plaintiffs remaining discrimination arguments. Plaintiffs first contend that the statute discriminates against interstate commerce because, in many cases, the assessment on out-of-state beef processors exceeds the equivalent of the $1.00 head fee imposed on California cattle. According to plaintiffs complicated calculations, the mil assessments on out-of-state carcass beef will exceed the equivalent of the $1.00 head fee whenever the original animal weighs more than 1,100 pounds. (Plaintiffs' Opening Brief, p. 58).

Defendants do not challenge the accuracy of plaintiffs' calculations, but argue that the problem is eliminated by Section 64713 which puts a ceiling on the mil assessments. Section 64713 reads in pertinent part as follows:

> [P]ersons subject to this assessment shall not be required to pay an amount in excess of the equivalent of one dollar ($1) per head. Any person who pays an assessment in excess of the equivalent of one dollar ($1) per head shall be entitled to a refund of the excess portion of the payment as long as the person demonstrates to the satisfaction of the director or his or her agent that a refund is warranted. The assessment provided in this Section is intended to be the equivalent of the fee provided in Section 64691.

Plaintiffs would have this Court rule that Section 64713 is a sham because it imposes on out-of-state beef processors who purchase beef the impossible burden of determining the weight of the live animal from which the carcass came.[13] This the Court declines to do. By virtue of this Court's duty to read statutes in the light most favorable to their constitutionality, *Ashwander v. Tennessee Valley Authority*, 297 U.S. 288, 348 (1936), this Court interprets Section 64713 as permitting the director to require only that degree of proof which is reasonable under the circumstances. Thus understood, Section 64713 provides satisfactory protection against compulsory overpayments by out-of-state beef processors.[14]

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[13]The Court takes note of, but does not base its decision on, proposed regulations which make clear that the documentation burden imposed on out-of-state beef processors is a reasonable one. Proposed Section 2252(e)(1) eliminates the tracing problem by permitting out-of-state beef processors to compute their refund based on the average live weight and average yield of beef shipped into the state.

[14]Plaintiffs present another argument which is an offshoot of their first and warrants like disposition. Plaintiffs argue that because over eight percent (8%) of the value of a single animal is contained in parts other than beef carcass, out-of-state processors who

The Court is also mindful of the fact that plaintiffs have tried to shift the focus of inquiry from the level of comparing the burdens on in-state and out-of-state industries to that of individual processors. When the focus is properly returned to a comparison of the two industries, there is no doubt that Californians continue to shoulder more than their fair share of the costs of the Beef Council's programs. The parties have expressly stipulated to the fact that:

> [A]t least half of the cattle in California change hands more than one time before slaughter. Consequently, more than one California Beef Council fee is usually paid on a given animal during its lifetime.

Stip. #30. Thus, in practice the maximum fee on out-of-state beef corresponds to the minimum fee on California cattle.

The same conclusion is reached by comparing the percentage of out-of-state beef consumed in California with the percentage of Beef Council funds out-of-state beef processors are expected to generate. Sixty percent (60%) of the beef consumed in California is produced in other states (Stip. #27). The 1982 amendments are expected to result in annual revenues of $5.3 million dollars (Stip. #10). Since the pre-1982 head fees generated $800,000.00 dollars per year (Stip. #26) and the rate was quad-

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purchase beef pay more than their fair share. In other words, it is discriminatory to impose the equivalent of a $0.92 head fee on local cattle and a $1.0 head fee on out-of-state beef. Again, because the statute does not preclude an appropriate reduction in the special case of an out-of-state beef processor who purchases beef, this Court is not prepared to invalidate the statute on this ground. The Court also notes that Section 2252(e)(3) of the proposed regulations permits out-of-state processors who purchase beef to reduce the total assessment by eight percent (8%).

rupled, the new head fees can be expected to generate $3.2 million dollars annually. Thus, the mil assessments are expected to generate $2.1 million dollars, or forty percent (40%) of the total revenues. Since out-of-state processors account for sixty percent (60%) of the beef consumed in California but pay for only forty percent (40%) of the Beef Council's activities, it is undeniable that out-of-state processors are paying substantially less than their fair share of the load.

Plaintiffs present two other arguments which are likewise unpersuasive to the Court. The first contends that the California Beef Council may be improperly subsidizing the California Bureau of Livestock Identification. This amounts to a simple *utlra vires* argument which is not encompassed by the Commerce Clause. The second argument alleges that California beef produced from a totally integrated local operation may entirely escape Beef Council assessments. This argument is based on the following provision:

> The fee which is required by Section 64691 shall be paid for each head of cattle which is slaughtered in the state unless it is specifically excepted by Section 64691. If the fee is not otherwise deducted from the seller as provided in Section 64691, it shall be paid by the *purchaser or slaughterer* and is due and payable in the manner provided in Section 64617.

Section 64692 (emphasis added). Plaintiffs interpret Section 64692 to mean that a fee is imposed only when cattle are sold at slaughter.

Plaintiffs' interpretation is contrary to the plain meaning of the statute and the interpretation of the state agency charged with its enforcement. The first sentence plainly con-

templates payment of head fees at the time of slaughter and does not limit the payment requirement to animals sold at that time. The phrase "purchaser or slaughterer" in the second sentence explicitly communicates the idea that payment is required even if no sale takes place. Moreover, the Food and Agriculture Department, the agency responsible for this statute's enforcement, interprets this provision as requiring payment of a fee on every animal slaughtered in California regardless of whether the animal was sold before slaughter. Declaration of Mr. Hans Van Nes, Deputy Dir. of Cal. Dept. of Food & Agric., p. 2, ¶ 5, Defs.' Exh. #6. For the above reasons, the Court rejects plaintiffs' interpretation as wholly lacking in merit.

## IV. THE EQUAL PROTECTION CLAUSE

Plaintiffs argue that the fact that out-of-state beef processors are required to support the California Beef Council but are denied representation on the Council violates the Equal Protection Clause. While it is true that members of the Beef Council must be California residents, § 64591 and thus out-of-state beef processors may not serve on the Council, it does not follow that the rule violates the Equal Protection Clause. Where, as here, the statute under attack does not adversely affect a suspect class of persons or a fundamental constitutional right, the statute must be deemed irrational before it may be ruled unconstitutional. *Williamson v. Lee Optical of Oklahoma,* 348 U.S. 483 (1955). Here the limitation of membership to California residents is clearly not irrational. The state legislature may have rationally concluded that the interests of out-of-state processors were already adequately represented by the statutory re-

quirements that two of the twenty-one representatives be slaughterers. Moreover, the state legislature may have rationally decided that the administrative burden of seeking nominations from persons throughout the nation would be too heavy and therefore impractical.

For the reasons as stated herein, plaintiffs' motion for summary judgment is DENIED, and defendants' cross-motion for summary judgment is GRANTED.

IT IS SO ORDERED.

DATED: April 20, 1983.

RAUL A. RAMIREZ
Raul A. Ramirez, *Judge*
United States District Court

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT
No. 83-1979
District Court
No. CIV S-82-194 RAR
National Meat Association,
American Meat Institute, et al.,
Plaintiffs-Appellants,

vs.

George Deukmejian, et al.,
Defendants-Appellees.
Filed October 5, 1984

# NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

NOTICE IS HEREBY GIVEN that Defendants George Deukmejian, Governor of the State of California, John K. Van De Kamp, Attorney General of the State of California, and Clare Berryhill, Director of the California Department of Food and Agriculture, hereby appeal to the Supreme Court of the United States from the judgment of the United States Court of Appeals for the Ninth Circuit, entered in this action on September 21, 1984.

This appeal is taken pursuant to 28 United States Code section 1254(2).

DATED: October 5, 1984

JOHN K. VAN DE KAMP
Attorney General of the
State of California
R. H. CONNETT
Assistant Attorney General
RODERICK E. WALSTON
ALLENE C. ZANGER
Deputy Attorneys General

/s/ RODERICK E. WALSTON
Roderick E. Walston
Deputy Attorney General
*Attorneys for*
*Defendants-Appellees*